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STATEMENT OF
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BEFORE THE
SUBCOMMITTEE ON DOMESTIC MARKETING, CONSUMER RELATIONS AND NUTRITION
COMMITTEE ON AGRICULTURE
UNITED STATES HOUSE OF REPRESENTATIVES
July 25, 1978

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to appear before the House Agriculture Subcommittee on Domestic Marketing, Consumer Relations and Nutrition, to discuss the role of food prices in inflation and the overall impact of food price increases on the public.

The Department of Agriculture is pleased to be a part of these hearings. We are committed to the implementation of a national food policy. That policy we believe must have as its basic premise the assurance that there will continue to be an adequate, safe, wholesome, nutritionally balanced food supply available to all Americans at prices that are fair to consumers and producers. Basic to reasonably priced food in the future is an adequate return to food producers.

A wide range of programs now being administered by various agencies within the Department of Agriculture reflect our commitment to make such a policy work, programs that exert an influence on all sectors of the food system--consumers, producers and food marketing firms. They include the commodity price and farm income support programs designed to insure the financial stability, and thus continued productivity of farmers; the meat and poultry inspection programs designed to safeguard the food supply; and the food and nutrition programs designed to make certain that those financially disadvantaged are still able to eat well.

A national food policy must address the interests of all of our citizens. Let me say at the outset that a cheap food policy is not a bargain for anybody. Unless the farm and food marketing sectors are economically viable the most basic element of our food policy--adequate food supplies--will not be satisfied. This Administration does not support the concept of cheap food.

Let me also assure you that this Administration is very concerned about the real hardships the rapidly rising food prices this year are causing. Inflation--and particularly food price inflation--is a tax on us all. It is regressive, affecting most severely those least able to bear it. Undoubtedly, many Americans, particularly the elderly and those on fixed incomes, are being forced to adjust their eating habits in order to make ends meet.

It is my understanding that the Committee is particularly interested in hearing some discussion of the following: the role of food prices in inflation generally, the impact of the recent food price increases on various sectors of the public at large, and the actions we are taking to discourage and prevent unnecessary increases in food prices. Following this, I will make a few comments about prospects for the rest of the year, and then attempt to answer any questions you may have.

I. The Role of Food Prices in Inflation

Retail food prices are monitored and reported monthly by the Department of Labor. The reports for each month are released near the end of the subsequent month. For example, the Consumer Price Index (CPI) for June will be released near the end of July.

The food prices used to develop the CPI are collected for a wide variety of food products. These prices are summarized, weighted by their relative importance, and reported in the form of index numbers for the major product groups.

The relative importance of food in the overall CPI is now about 18 percent—reflecting that, on the average, about 18 percent of the consumer dollar is for the purchase of food (Table 1). Consequently, a 10 percent increase in food prices in any one year would result in an increase of 1.8 percent in the overall Consumer Price Index, assuming the prices for all other items are unchanged. In importance of expenditures, food ranks only below shelter (29.18 percent) and transportation (18.03 percent).

The food category is subdivided into two major components: the food-at-home category with 12.2 percent weight in the CPI, and away-from-home category with a 5½ percent weight.

The relative importance of each commodity category in the food-at-home index is also shown in Table 1. These weights reflect the food-at-home expenditures of the average U.S. household during 1973 and 1974 (the most recently available base).

Meat prices account for more than 32 percent of the overall at-home-food price index. This means that if retail meat prices go up by about 20 percent this year (as we now expect they will), meat prices alone will contribute 6½ percent to the overall at-home-food price increase. Other important product groups include fruits and vegetables (14.4 percent), dairy products (13.5 percent), and cereal and bakery products (12.5 percent). Often neglected as food categories, but increasingly important, are nonalcoholic beverages such as coffee, tea, and soft drinks (12.4 percent), and other prepared foods (8.5 percent).

Knowing the importance of these various components helps one understand how price changes in one area (meats, for example) influence our measure of food prices overall more than the same change in another area (like fats and oils products). I now turn to the question about the contribution of food prices to overall price inflation.

Examining the historical year-to-year changes in retail food prices reveals that in 17 of the 27 years since 1950, food prices contributed less than 1 percentage point to the overall rate of inflation (Table 2). In four of those years, 1953, 1954, 1955 and 1959, food prices actually reduced the overall rate of inflation in the economy.

It is important to note, however, that four of the largest year-to-year percentage changes in retail food prices occurred during the five years since 1972. Only once since then (in 1976) have food price increases contributed less than 1 percentage point to the overall inflation rate.

The inflationary effect of the changed input price situation during the years since 1965 cannot be ignored. Marketing costs account for approximately 60 percent of the retail cost of our domestically produced farm foods. The recent increased cost of energy inputs in particular, has contributed significantly to the increased level of food prices in recent years. For example, during the period from September 1973 to May 1974, food prices increased at a much faster rate (17.9 percent) than nonfood commodities (11.1 percent) but at a much slower rate than price increases for energy products (62.1 percent).

In addition, the recent volatility in prices of foreign foods and fish have had a significant effect. These foods account for about 11 percent of the food-at-home index. In the years since 1970, prices for these products have increased 145 percent. Retail prices for the domestically produced farm foods, on the other hand, have increased 58 percent. The effect of the increases in this category was most obvious in 1977 when food prices increased by 6.3 percent largely because of price increases for coffee.

These data clearly indicate that, while food prices have contributed to the general inflationary pressures in some years, food prices have not been consistent nor prominent contributors to the overall inflation problem.

Table 1. Relative Importance of Food Groups in the Consumer Price Index,
December 1977.

Consumer Price Index--All Urban		
	Percent	
Food	17.718	
Food at home	12.235	100.00
Cereals and bakery products	1.530	12.51
Meats, poultry, fish and eggs	3.943	32.22
Dairy products	1.654	13.52
Fruits and vegetables	1.759	14.38
Sugars and sweets	0.435	3.56
Fats and oils	0.360	2.94
Nonalcoholic beverages	1.513	12.36
Other prepared foods	1.041	8.51
Food away from home	5.483	

Source: U.S. Department of Labor, Bureau of Labor Statistics

Table 2. Contribution of Food Prices to Inflation.

Year	Change in Food Prices	Contribution to Overall Inflation
	(Percent)	(Percentage Points)
1950	---	---
1951	+11.1	+2.7
1952	+ 1.8	+ .4
1953	- 1.5	- .4
1954	- .2	- .1
1955	- 1.4	- .3
1956	+ .7	+ .2
1957	+ 3.3	+ .8
1958	+ 4.2	+1.0
1959	- 1.6	- .4
1960	+ 1.0	+ .2
1961	+ 1.3	+ .3
1962	+ .9	+ .2
1963	+ 1.4	+ .3
1964	+ 1.3	+ .3
1965	+ 2.2	+ .5
1966	+ 5.0	+1.2
1967	+ .9	+ .2
1968	+ 3.6	+ .9
1969	+ 5.1	+1.2
1970	+ 5.5	+1.3
1971	+ 3.0	+ .7
1972	+ 4.3	+1.0
1973	+14.5	+3.5
1974	+14.4	+3.5
1975	+ 8.5	+2.0
1976	+ 3.1	+ .8
1977	+ 6.3	+1.5
1978 (P)	+8 to +10	+1.4 to 1.8

Food prices in any one year are determined largely by the conditions which prevail in three general areas:

- The farm production sector (product availability)
- The marketing sector
- Consumer purchase conditions

Farm Production, Farm Prices and Retail Prices for Food

The years since 1950 have shown some rather dramatic year-to-year changes in farm product prices (Figure 1). Commodity prices, as you know, are largely determined by what is produced, both on U.S. farms and worldwide. What is produced on farms in any one year is heavily influenced by rather unpredictable natural forces such as weather, pest infestations, and plant and animal diseases. These occurrences are almost impossible to forecast. But with the help of the Congress, we are making progress to safeguard consumers and farmers against the disruptive fluctuations in price which result from such natural disasters.

The 1977 Food and Agriculture Act included provisions for the establishment of a grain reserve. A farmer-owned reserve program for wheat is mandated, with terms and conditions essentially identical to the program announced by the Administration in April 1977 using existing authorities.

We plan to have a 30 to 35 million metric ton (MMT) managed reserve composed of: (a) farmer-owned stocks and (b) up to 6 MMT of government owned stocks to assure our ability to fulfill food aid commitments (International Emergency Wheat Reserve). Significant progress has been made toward the realization of this goal. At the present time we have about 10 MMT of farmer-held wheat stocks in the reserve program, and just over 4 MMT of farmer-held feed grains. The target is to have the farmer-owned feed grain reserve in place by October 1. We have yet to accumulate the amount needed for the International Emergency Wheat Reserve.

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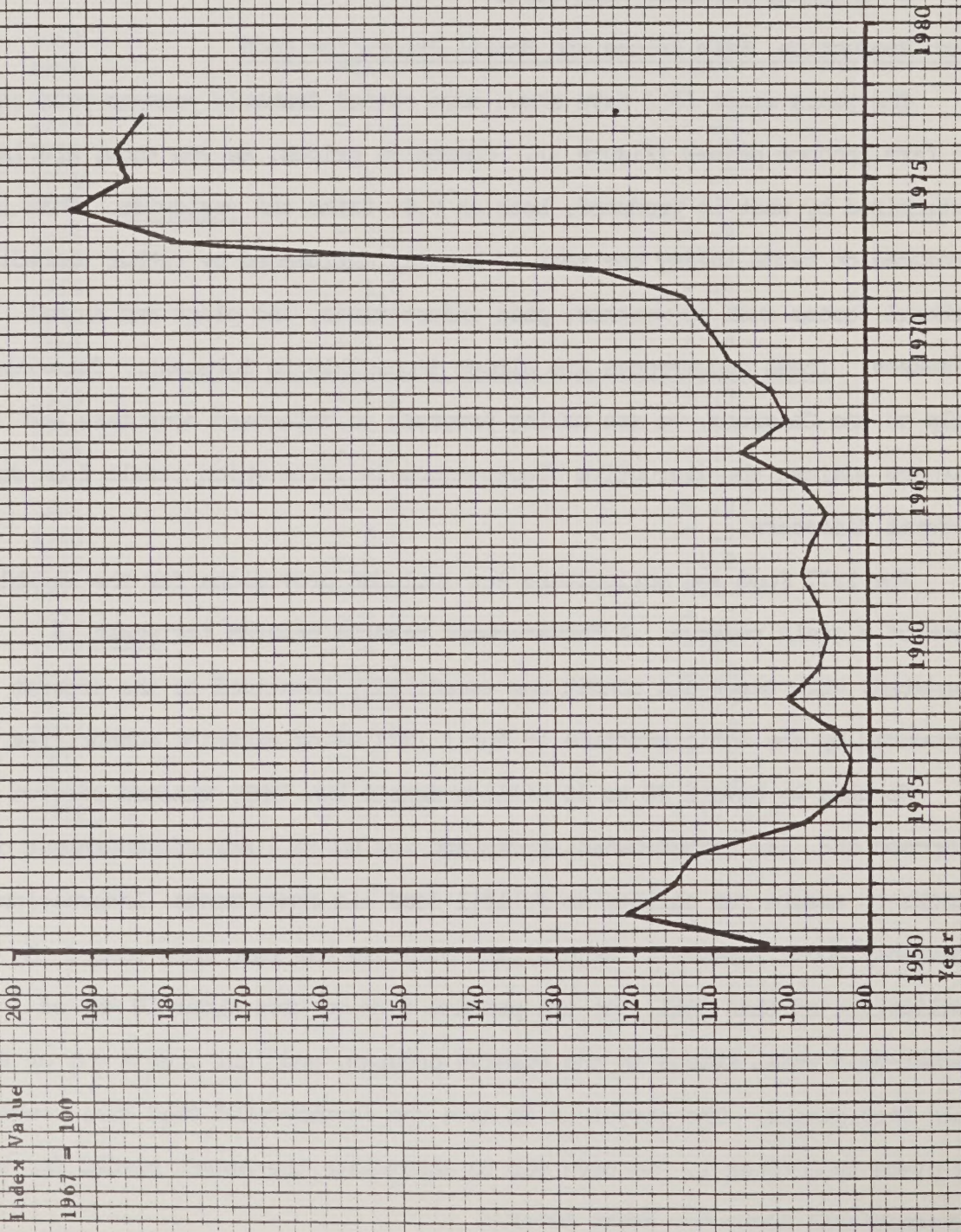


Figure 1. Index of Prices Received by Farmers, 1950-77.

The formation of these managed reserves, with specific operating rules, dramatically changes the structure of our national grain holding policy of the last quarter century. We have had stocks before. They were often much larger than we wanted. But, they were not held in an organized reserve, with specific mechanisms to allow for their release into the market when needed. Today, the likelihood that we will see extreme grain price changes, like those that occurred in 1972, is significantly reduced as a result of this action.

Weather conditions affect the production of other farm products. 1978 is an excellent example. Severe cold in the hog producing states last winter, and the reduction in the cattle inventory since 1975, were to a large extent, the most important factors responsible for the rapid increase in meat prices this year. Early indications from producers were that pork production this year would be up about 10 percent during 1978. When the USDA Hogs and Pigs Report was released on March 20 of this year, we learned that farrowings were actually down 1 percent. Several factors influenced producers decisions, including the cold weather during December, January and February that caused breeding and farrowing problems for producers. We now expect total pork production this year to show little or no increase over last year. For the first time in recent history, poultry production per capita will exceed pork consumption.

This weather-related problem triggered a chain reaction in prices of other meats. Without the expected increase in pork supplies, pressure on the tight supplies of beef intensified. And, because broiler producers had been expecting the increased pork production (and associated lower prices), poultry prices increased faster than they otherwise would have.

Also, after a period of drought, the rains came to California. In the process, planting schedules for some vegetables were disrupted. Lettuce prices, in particular, rose to record levels in response to the limited available supplies. Prices for lettuce, which usually range from \$2.50 to \$5.00 per crate of 24 heads, increased to \$18.00. Frost damage and cool weather earlier in the year adversely affected the production of tomatoes and other vegetables in Florida and the Rio Grande Valley in Texas.

There are, in addition, biological and genetic realities to deal with in producing agricultural products. In many cases, it is simply impossible to increase the production of one food product when another has been adversely affected by weather. For example, 27 months are required from the time a beef cow is bred until the offspring reaches slaughter weight. Furthermore, if the first offspring is retained to increase the herd (the production plant), it could be $5\frac{1}{2}$ years from the time the first calf is retained until the first offspring reaches slaughter (Figure 2). For the hog producer, this adjustment period is much shorter, about $2\frac{1}{2}$ years. Broiler production, on the other hand, can be increased in about a 3-month period.

The forces of the cattle cycle have been particularly evident during the past decade. Beef producers responded to favorable cattle prices during the late 1960's and early 1970's and expanded their cattle herds. The expansion continued, due to biological thrust, after prices declined to unfavorable levels for producers. The total cattle and calf inventory increased from 108.8 million head in 1967 to a record 132 million in 1975. Meanwhile, the beef cow herd increased from 33.8 million head to 45.7 million (Figure 3). Now, the cattle herd is much smaller, down from the 132 million in 1975 to 116.3 million at the beginning of this year. The beef cow herd is down from 45.7 million in 1975 to 38.7 million. Beef production is declining and further declines are anticipated as herd rebuilding gets underway again.

FIGURE 2. PRODUCTION LAGS DUE TO BIOLOGICAL LAGS

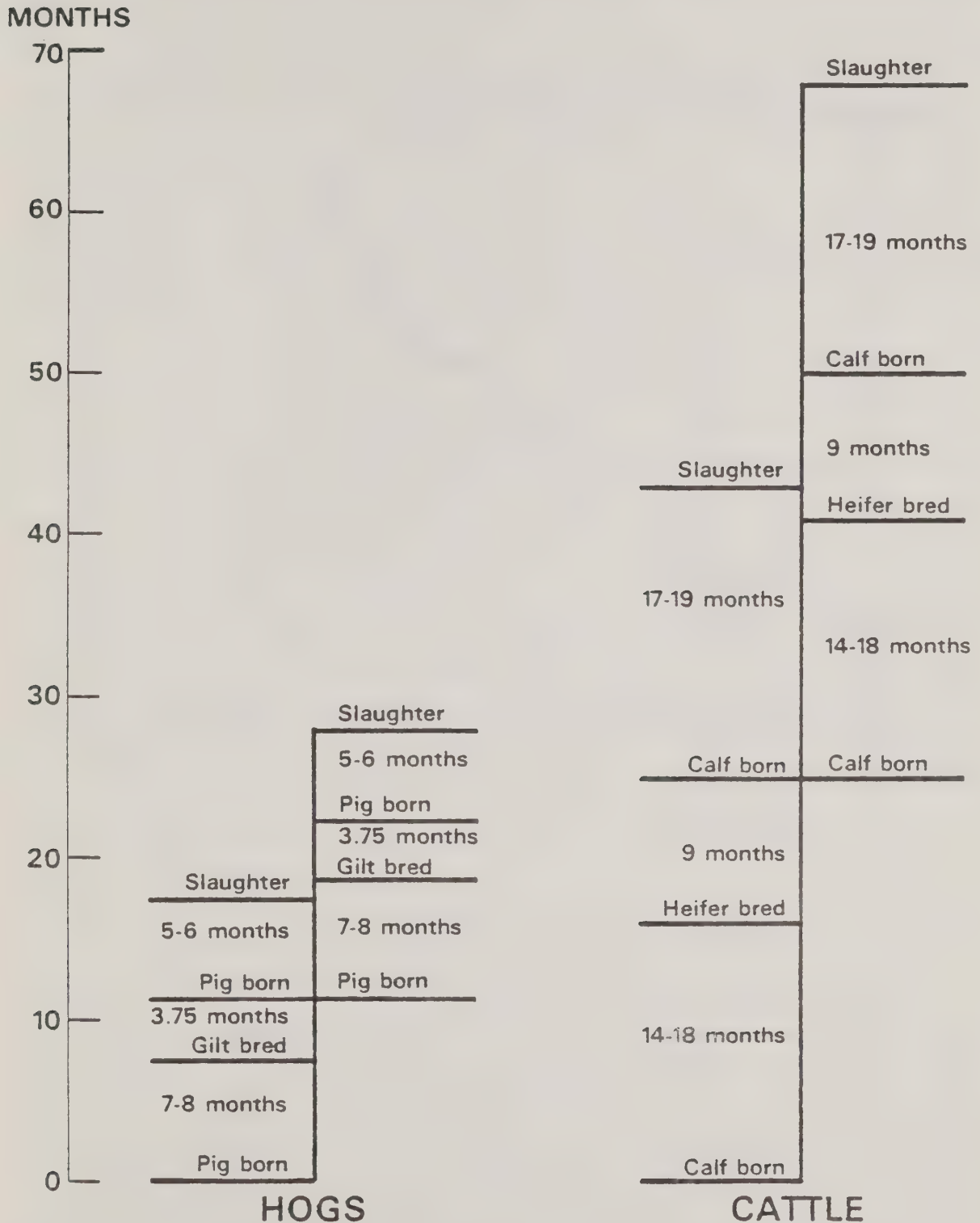
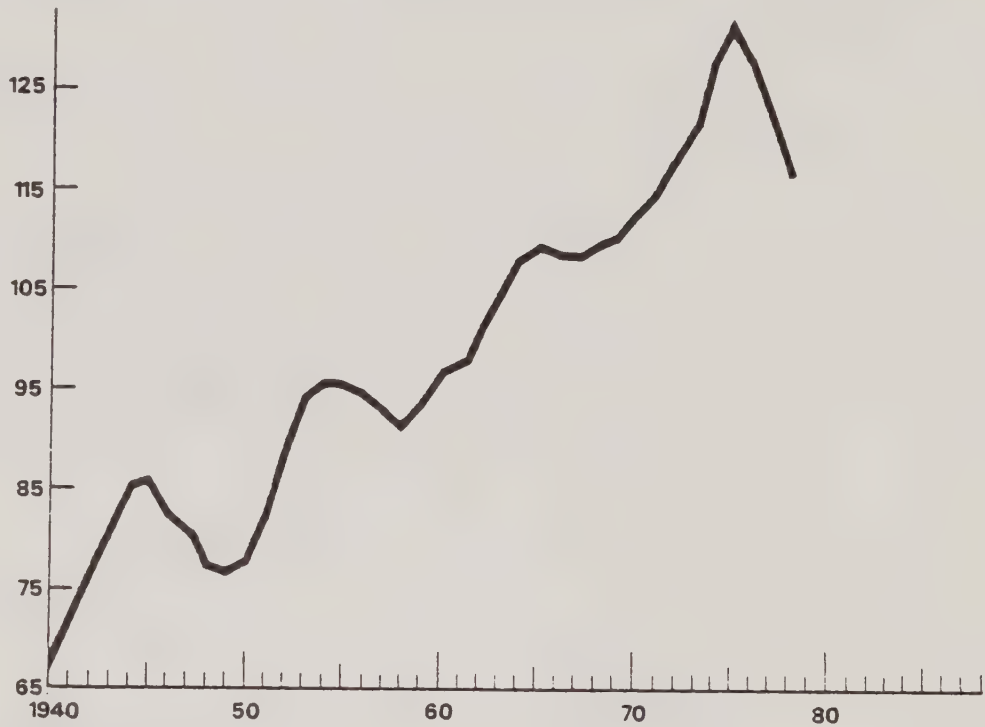


FIGURE 3. CATTLE ON FARMS, January 1

Mil. Hd.



USDA/ESCS

May 1978

Given the uncertainties with the weather, as well as the biological and genetic constraints, it should not be surprising that farm product prices are quite volatile from year to year. But what about the relationship between food prices and farm prices? Do consumer prices respond to the changes in raw product prices?

In general, the answer to that question is that they do respond. The data plotted in Figure 4 verify that there is a correspondence between changes in food prices and changes in prices for farm products.

But retail price changes over the years have not been as volatile as the year-to-year percentage changes in farm prices. In almost every case, there was a smaller percentage change in the index of retail food prices than there was in the index of prices received by farmers. Retail prices did not go up as fast as farm prices but they did not fall as fast either.

Since 1950, changes in retail food prices have averaged 3.65 percent per year. But this really reflects three rather distinct periods: During 1950 to 1959, retail price changes averaged 1.7 percent; in the 1960's, retail price changes began to trend upward at an average rate of 2.7 percent per year; and since 1970, average year-to-year changes in retail food prices have averaged 7.7 percent.

Some care must be exercised when making comparisons of the movements in these two indices since they do not include the same items and relative importances are different. Various nonfood items such as cotton and tobacco are included in the index of prices received by farmers. In addition, the prices of all grains are included in the farm price index even though relatively small quantities are used directly in food products. The retail index contains prices for the foreign foods and fish as well as the cost for foods consumed away from home.

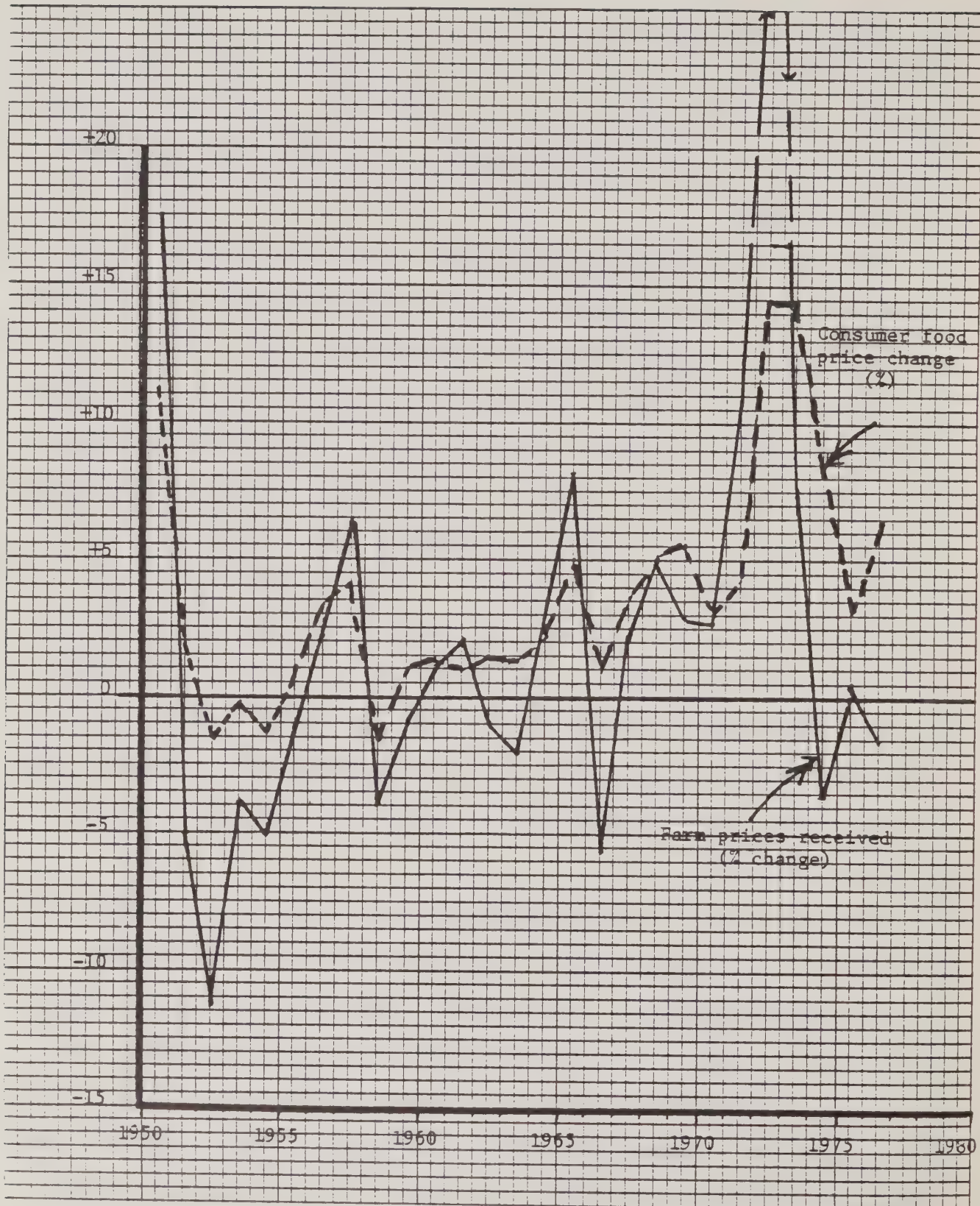


Figure 4. Percentage Change in Farm and Retail Food Prices, 1950-77.

Even so, the data make it clear that average changes in the index of prices received by farmers have been much more volatile than year-to-year changes in the index of retail food prices.

Since 1960, the index of prices received by farmers has not trended upward like retail food prices have. This changed nature of the relationship between farm prices and food prices, particularly since about 1960, is a reflection of the fact that retail food prices are increasingly influenced by the changing costs of transporting, processing, and marketing food and by changing conditions which influence consumer food choices.

Marketing Sector Costs

Changes in the cost of processing, transporting and selling food products are monitored by USDA. The data are referred to as the "marketing bill."

The bill for marketing food has increased each year from \$31.5 billion in 1953 to a projected \$135 billion in 1978, an increase of 328 percent (Table 3). This change includes the cost for marketing a steadily increasing quantity of food, but there have been increases in the per unit costs of marketing food, too. In 1950 payments for marketing costs were $1\frac{1}{2}$ times the farm value of the personal consumption expenditures for food. Today marketing costs are more than twice the farm value.

Changes in the relative importance of the various components of the marketing bill indicate that prices of some marketing inputs are changing more than others and that the relative usage of these inputs are also changing (Table 4). These changes imply changes in the product mix being marketed.

Since 1963, labor, packaging, and profits have all trended upward as a percent of the total marketing bill for foods. The percent changes in these components is greater than the year-to-year percent changes in retail food prices. Labor is the major contributor to food marketing costs, accounting

Table 3. The Bill for Marketing Food, 1950-1976.

Year	Total Consumer Expenditures	Marketing Bill	Farm Value
(Million Dollars)			
1950	43,992	25,960	18,032
1951	49,252	28,740	20,512
1952	50,932	30,519	20,413
1953	51,013	31,553	19,460
1954	51,140	32,316	18,824
1955	53,127	34,378	18,749
1956	55,548	36,302	19,246
1957	58,293	37,888	20,405
1958	60,993	39,548	21,445
1959	63,619	42,404	21,215
1960	66,881	44,566	22,315
1961	68,672	45,674	22,998
1962	71,317	47,656	23,661
1963	74,044	49,895	24,149
1964	77,503	52,631	24,872
1965	81,114	54,001	27,113
1966	86,923	57,156	29,767
1967	90,229	61,410	28,819
1968	93,983	63,570	30,412
1969	97,765	64,097	33,668
1970	105,951	71,177	34,774
1971	110,758	75,440	35,318
1972	117,872	78,524	39,348
1973	135,337	84,215	51,122
1974	149,239	93,229	56,010
1975	161,385	106,464	54,921
1976	172,346	115,997	56,349
1977 (P)	182,000	125,000	57,000
1978 (E)	201,000	135,000	66,000

Source: USDA/ESCS

Table 4. Changes in Importance of Selected Components of the Food Marketing Bill, 1963 to 1976

Year	Labor	Packaging	Transportation	Profits Before Taxes	Advertising
(Percentage)					
1963	42.72	11.82	8.42	4.81	2.62
1964	41.99	11.40	8.17	5.32	2.61
1965	43.22	11.48	7.78	5.56	2.59
1966	43.10	12.07	7.35	5.95	2.57
1967	42.17	11.72	7.00	5.54	2.49
1968	44.06	12.27	7.08	5.66	2.48
1969	47.44	12.48	7.18	5.62	2.57
1970	45.41	12.79	7.31	5.06	2.37
1971	45.68	12.86	7.95	5.17	2.29
1972	47.94	12.99	7.77	5.09	2.34
1973	48.34	12.94	7.12	6.41	2.18
1974	48.06	12.98	7.72	6.65	2.29
1975	46.03	12.59	7.80	7.61	2.21
1976	47.74	12.93	8.19	7.07	2.12

Source: USDA/ESCS

Table 4a. Annual Percent Changes in Selected Cost Components of the Food Marketing Bill, 1966 to 1977

Year	Labor	Packaging	Transportation	Corporate Profits Before Taxes
(Percentage)				
1967	5.3	8.7	2.4	N.C.
1968	8.1	9.3	4.7	5.9
1969	8.6	3.7	2.2	N.C.
1970	6.3	7.1	13.0	N.C.
1971	6.8	6.6	15.4	22.2
1972	9.0	5.2	1.7	-9.1
1973	8.0	6.9	-1.6	35.0
1974	10.3	11.0	20.0	14.8
1975	9.6	17.4	15.3	30.6
1976	10.6	11.3	14.5	N.C.
1977 ^{1/}	8.5	7.0	10.0	-2.4

^{1/} Preliminary.

N.C. = No Change.

Source: USDA/ESCS

for 45 to 48 percent of the total bill in recent years. The size of the labor component was about \$60.0 billion in 1977. Costs for labor have been increasing at a rate of 10 percent per year since 1974.

Packaging costs are the second most important component, fluctuating between 12 and 13 percent of the total. Packaging cost consumers \$16 billion in 1977, up from \$5.9 billion in 1963. Year-to-year percent changes in packaging costs have also been greater than 10 percent since 1974.

The proportion of the food marketing bill accounted for by transportation costs has also increased since 1967, although the change in its share of the bill was only about 1 percent of the total. This is a sizeable increase compared to some components, but low relative to the 4 percent share increase of labor. Here again, the annual percent changes have exceeded 10 percent since 1974. The total cost of transportation in the food marketing bill was \$9.0 billion in 1977.

Profits (before taxes) have increased steadily as a proportion of the bill up to 7 percent of the total, about \$8 billion.

Advertising, a small but controversial marketing cost (2-3 percent), has shown a slight decrease in relative value in recent years. Even so, the cost of food advertising was 88 percent greater in 1976 (\$2.46 billion) than in 1963 (\$1.31 billion).

Increased costs for these inputs continue to put upward pressure on food prices this year. In the first quarter of this year hourly earnings in food processing and distribution averaged 3 percent above the fourth quarter and 8.9 percent higher than a year earlier. In addition to labor costs, price increases for a wide array of other inputs (fuels, packaging supplies, rent, etc.) are increasing at an annual rate of about $7\frac{1}{2}$ percent. Natural gas prices, for example, are expected to rise 10 to 20 percent this year.

Transportation costs are also increasing food marketing costs this year. Railroad freight rates for shipping food products were relatively stable for the first 5 months of 1978 after posting a 5 percent increase in December 1977. But effective June 17 freight rates increases of 2 to 4 percent were granted by the ICC. Earlier this year, the ICC allowed truck freight rate increases ranging up to 7 1/2 percent.

Profits in the first quarter of 1978 averaged 11.4 percent of equity, compared with 13.6 percent in the fourth quarter of 1977 and 11.4 percent a year earlier.

The increasing cost of transforming raw farm products to food ready for consumers reflects increases in input costs similar to those in other products.

Each of these marketing functions must be performed and, each has a cost. The demand for food is much more than a demand for raw farm products; it is also a demand for services.

Conditions Affecting Consumer Food Choices

Ultimately, the food system exists for consumers. Therefore, the system must be responsive to changes in the tastes and preferences for foods. Changing lifestyles, smaller family units, improved economic conditions, and the increased number of multiple wage-earner households have undoubtedly influenced the changes we have witnessed in eating habits. While advertising does play a role in the food selection process, the growth in the consumption of highly processed convenience foods (foods with a relatively low farm value) would not have been possible without consumer acceptance of such products.

Population growth is often considered when people discuss retail food demand, but it is also important to consider how the composition of the population is changing as well.

During 1950 to 1955, the U.S. population grew by 9 percent. The number of persons under 5 years of age increased 13.10 percent, and the number between 5 and 13 increased by 24.5 percent (Table 5). The growth in these two age categories during this period reflected the post-World War II baby boom. The number of individuals 65 years and over also grew at a rate greater than total population during this same period.

In comparison, during 1970 to 1975, the number of persons in the younger age groups declined by about 7 1/2 percent. Total U.S. population during the period increased by 4.2 percent. Increases occurred in the number of individuals in the age groups, 18 to 24, 25 to 34, and 65 years or over. Most of the growth in the 18 to 24 and 25 to 34 age groups between 1970 and 1975 can be attributed to the children born during the post-war baby boom.

The maturing of the post-World War II babies and the decline in the birth rate caused average per capita consumption of most food products to expand after 1960. To some extent, the overall effect of this increase was offset by an increase in the proportion of the population over 65 years of age, since these individuals tend to consume less of most food products than other adults.

Food products heavily consumed by persons in the under 5 years of age group have declined along with declines in the number of persons in that age group since 1960. One such food product is fluid milk. Between 1960

Table 5. Changes in the Percent of the U.S. Population in Various Age Groups, 1950 to 1975.

Age Group	Year Interval				
	1950 to 1955	1955 to 1960	1960 to 1965	1965 to 1970	1970 to 1975
Less than 5 years	+13.1	+ 9.6	- 2.5	-13.5	- 7.4
5 to 13 years	+24.5	+18.0	+ 8.5	+ 2.5	- 8.7
14 to 17 years	+ 9.5	+21.3	+26.2	+12.4	+ 6.4
18 to 24 years	- 6.9	+ 7.7	+25.8	+21.6	+11.8
25 to 34 years	+ 1.0	- 5.6	- 2.0	+12.6	+22.2
35 to 44 years	+ 5.9	+ 5.7	+ 0.9	- 5.3	- 1.4
45 to 54 years	+ 8.2	+ 9.0	+ 6.1	+ 6.7	+ 1.9
55 to 64 years	+ 9.2	+ 6.9	+ 9.3	+ 9.3	+ 5.9
65 and older	+17.2	+14.8	+10.7	+ 8.9	+11.5
Total U.S.	+ 9.0	+ 8.9	+ 7.5	+ 5.4	+ 4.2

Source: U.S. Department of Commerce, Bureau of Census, Current Population Reports, Series P-25, No. 704, July 1977.

and 1976, per capita fluid milk consumption declined by over 30 percent.

The overall effect such changes in demand have had on retail food price increases since 1950 is difficult to assess. But clearly, they do affect prices. The effect is most pronounced when changes in the make-up of the population result in a relatively higher proportion of people in age groups typically consuming foods like meat, which can be important contributors to overall food price changes.

II. The Impact of Food Price Increases on the Public

Food price increases are highly visible. Food purchases are made weekly, sometimes daily. Thus, food prices contribute significantly to the inflation psychology of the public and receive disproportionate attention from policymakers. But it is important to keep the overall effect of food price inflation in perspective.

The overall effect of food price inflation on the American public can be partially assessed by reviewing the relationship between income and food prices. The average percent of U.S. total disposable personal income since 1950 spent on food has decreased from 22.2 to 16.8 percent (Table 6). While this percentage decline masks the effects of food price increases on different groups in the population, it does indicate that, in general, incomes have been increasing at a faster rate than retail food prices.

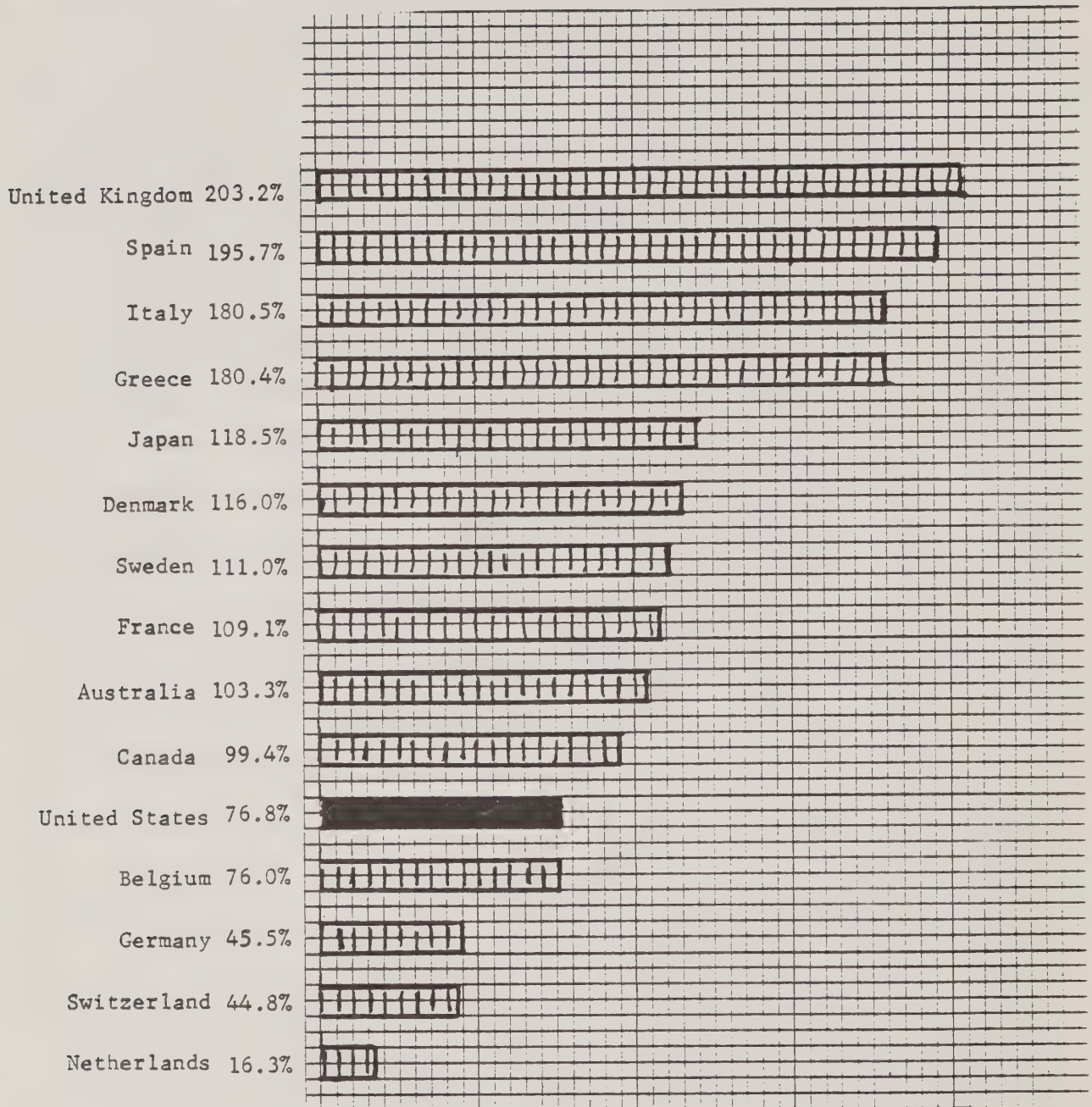
Another way of looking at the overall impact of food price increases is to compare what has happened here in the U.S. with what is happening around the world (Figure 5). Since 1970, retail food prices in the United States have increased at a slower rate than in 10 of the 15 countries surveyed by USDA's Foreign Agricultural Service. Only West Germany, the Netherlands,

Table 6. Percent of Income Spent for Food, Selected Years.

Year	Total Disposable Personal Income	Personal Consumption Expenditures for Food	Proportion of Disposable Personal Income
	(Billion Dollars)		(Percent)
1950	206.9	46.0	22.2
1955	275.3	58.1	21.1
1960	350.0	70.1	20.0
1965	472.2	85.8	18.2
1970	685.9	118.6	17.3
1971	742.8	122.0	16.4
1972	801.3	130.6	16.3
1973	901.7	146.8	16.3
1974	984.6	166.9	16.9
1975	1,084.4	184.8	17.0
1976	1,185.8	199.5	16.8
1977	1,309.2	218.4	16.7

Source: U.S. Department of Commerce

Figure 5. Percentage Increases in Food Prices, 1970 through March 1978



Source: OECD Main Economic Indicators, June 1978

Switzerland and Belgium showed lower rates of increase, and their prices are well above those in the United States.

However, through March of this year, five of the nations, including Japan and the United Kingdom have shown smaller food price advances than the U.S.

But we must also look at the distributional impacts of food price increases. The American food system is market-oriented. The available products are rationed in the marketplace to those with the financial resources to effect an exchange. Those with limited financial resources are hurt more by food price increases. Data indicating the proportion of total income spent for food by income class help identify the distributional effects of food price inflation.

The Department of Labor's Consumer Expenditure Survey for 1973/74 helps define the boundaries of this problem. Table 7 summarizes the proportion of total income spent for food for all U.S. households. The income group reporting less than \$5,000 pre-tax income per year earned 6.47 percent of all income, accounted for 15.38 percent of all food expenditures and totaled 18.17 percent of the population. The importance of food as an expenditure class is evident. Except for the highest and lowest income groups, the percent of the population in that group is roughly equivalent to the percent of the total expenditures made by that group (Figure 6).

Weekly food expenditures per person totaled \$10.24 in the lowest income group and \$15.02 in the highest group. Households in the lowest income group spent almost 40 percent of their pre-tax income on food. Those in the highest income class spent 10 percent of their income on food.

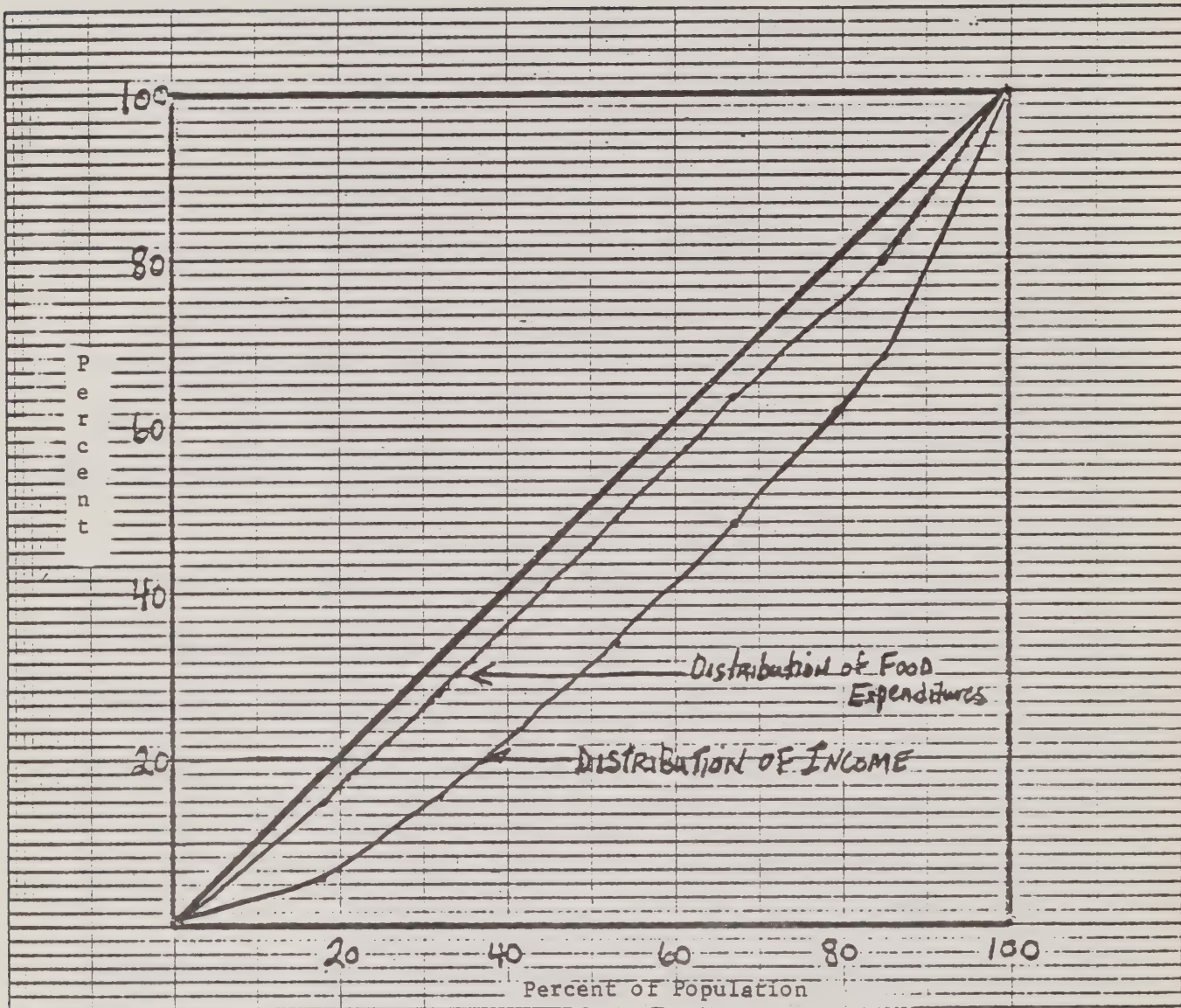


Figure 6. Distribution of Total Income and Total Food Expenditures by Percent of Population, 1973-74.

The effect of an approximate 10 percent increase in retail food prices, assuming no increases in prices of other items and no increases in income, is summarized by income class in Table 8. The lowest income households would have to reduce the proportion of their expenditures on nonfood items by about 4 percent in order to continue purchasing the same bundle of food items. Households in the higher income categories would only have to reduce the proportion of their expenditures on other things by about 1 percent. Alternatively, the quantity of food purchased would have to be reduced if purchases on nonfood items were to be maintained.

However, these assumptions are not very realistic. Most often prices of other items are increasing at the same time food prices are going up. Furthermore, the households in the higher income categories usually receive help because of increased incomes. Clearly, the burden of food price inflation falls disproportionately on the poor and those in the middle income groups. And if it were not for USDA's domestic food assistance programs, the problem would be much worse.

This Administration, with the Congress, has moved quickly to mitigate the burdensome effect of food price inflation on the poor. The 1977 Food Stamp Act contains important revisions designed to help those most in need of assistance obtain nutritious diets.

- The purchase requirement was eliminated--making it easier now for those with limited cash incomes to benefit from the program.
- The program was simplified so that the determination of eligibility is more straightforward, and
- The rules of eligibility were tightened so that higher income households are no longer eligible for benefits intended for those with the greatest need.

Table 8. Effect of a Ten Percent Increase in Retail Food Prices
by Income Class.

Income Class (1973 Dollars)	Percent Allocated to Other Items Would Have to be Reduced by:
Less than \$5,000	about 4 percent
\$5,000 to \$12,000	about 2 percent
\$12,000 to \$20,000	about 1.5 percent
\$20,000	about 1 percent

Table 7. Relationship Between Income and Expenditures for Food, 1973-74.

Income Class	Total Population	Total Reported Income	Total Food Expenditures	Food as a Percent of Income
(Percent)				
Less than \$5,000	18.19	6.47	15.39	38.88
\$5,000 to \$8,000	14.14	9.31	13.09	23.01
\$8,000 to \$12,000	21.17	17.79	20.35	18.72
\$12,000 to \$15,000	14.47	14.65	14.08	15.75
\$15,000 to \$20,000	16.07	19.86	17.29	14.26
Greater than \$20,000	15.96	31.92	19.80	10.17

Source: Data from 1973-74 Consumer Expenditure Survey, Bureau of Labor Statistics.

In addition, on July 1 the value of the allotment was adjusted to account for higher food prices. Allotment increases will average 4.4 percent. A family of four, for example, is now getting \$182 worth of stamps per month—\$8 more than previously. This adjustment is immediate relief for the more than 16 million persons now participating in the program each month.

III. Recent Actions

As I indicated at the outset, this Administration is concerned about the hardships caused by rapidly increasing food prices, particularly the disproportionate effect of such increases on the poor, the elderly and the others on fixed incomes. This concern is more than rhetoric. It has been translated into actions. But the actions we have taken have been carefully considered for their longer term impacts. Our approach is to try to eliminate basic problems rather than eliminating the symptoms of these problems.

Let me review with you some of the things we have done.

- Government farm price and income support programs

I have indicated that the most basic element of our national food and agricultural policy is the maintenance of an adequate long term supply of food. In order to achieve that objective, it is essential that we maintain the economic viability of American agriculture. We will continue to work with the Congress in the design, implementation and administration of farm price and income support programs. The importance of these programs to insure stable food prices must not be overlooked. As the analysis I have presented today indicates, food prices have increased most rapidly in those years when there have been shortfalls in agricultural production, either at home or abroad.

Working with the Congress, we have made significant progress in reducing the price impacts of government programs to support farm income. The new programs based on target prices and deficiency payments allow us to support farm prices at reasonable levels without unduly disrupting market prices. In years when the market price falls below the target price, deficiency payments are made to producers from the general tax revenue rather than from consumers of the food products being price supported. Under the old parity price—government purchase program, low income consumers of food were "taxed" like all others to help make price-support payments to farmers.

- Grain reserves

I want to re-emphasize the importance of the grain reserve program to farmers and consumers alike. This reserve allows us to accomplish two of our major goals: strengthening farm prices when there is a need and ensuring that we will have sufficient supplies to meet our domestic and international commitments in the event of poor crops.

The grain reserve program also provides needed price stability for our livestock sector. One of the reasons we are seeing rapid meat price increases today stems from the unprecedented grain prices during 1973/74 period. During that period, placements of cattle on feed dropped 17 percent below the high levels of 1971/72. In 1972, about 77 percent of the total commercial cattle slaughter came from feedlots. But by 1975, only 52 percent of the commercial cattle slaughter came from feedlots. In short, those high and erratic grain prices left U.S. cattlemen with little alternative but to liquidate their herds.

- Meat Imports

In early June of this year, the Administration decided to allow an additional 200 million pounds of imported meat into this country. The action was to help make certain that we did what we could to assure that adequate supplies of hamburger, hot dogs, and other processed meats were available while domestic cattlemen rebuild their herds.

Some have been critical of that decision saying that it put the rebuilding of the cattle herd in jeopardy. Statements have been made saying that the announcement of that decision on June 8 was responsible for the "dip" in the price of cattle during mid-June. The data simply do not support such allegations. Fed cattle prices have declined, but the steep decline did not come until after the June 13 release of the USDA Cattle on Feed report. Cattle prices then began rising in early July are now back to their early June levels. Clearly, the market is searching for a sustainable price level.

- The Sugar Program

The Administration opposes the current proposal to increase the support price of sugar to 17 cents per pound. The Administration is, of course, committed to the objective of maintaining a viable domestic sugar production sector, one that supplies a significant share of the domestic sweetener market. It is our basic belief that such a policy is in the long term in the best interest of the American people. It is important though that the increased support be provided by a means which takes into account the shorter term implications of the action on consumer prices.

Increases in sugar support price are quickly translated into higher retail prices for sugar and sugar based products. The increased importance of the nonalcoholic beverage category in the CPI, a category whose products use sugar as a major ingredient, makes it all the more important to be certain that our sugar policy does not act as an unnecessary fuel for food price inflation. Each 1 cent increase in the domestic support price for sugar adds at least \$300 million to sugar users expenditures. We must be certain therefore that our actions carefully consider the effect of these increased price supports on all food system participants.

- Food stamp benefits

As mentioned earlier, on July 1 the food stamp allotment was increased to help off-set the increased retail food prices. The adjusted allotments makes it possible for food stamp participant households to continue purchasing nutritious diets even in the face of the much higher retail food prices.

- Longer-run actions to make the market work more honestly

In addition to the items I've mentioned, we either have made, or are involved in making, a number of other decisions which we think will protect the integrity of the food system.

1. We are supporting research to investigate the effect of increased market concentration in the food system. Some recent studies have indicated that, in 1974, consumers paid about \$700 million more for food because some food markets were not as competitively structured as they might have been. While this is a large sum of money, it represents less than 1/2 of 1 percent of the total spent for food in that year. Regardless of the percentage, though, competition in food markets must be maintained if we are to assure consumers that prices don't increase

unnecessarily.

2. We have recently proposed net weight regulations for meat and poultry products. The proposed regulations require that: (a) the net weight be accurate at all points in the distribution chain from processing plant to the retail store; and (b) free liquid be excluded in determining the net weight. This proposal has generated a great deal of interest. It is clear that we must act in this matter since, in a time of high meat prices consumers must be assured of a fair value for the dollar spent.

3. We have also proposed new meat grading and labeling regulations. Both the meat marketing system in the United States and USDA's Federal meat grading program have been subject to various forms of corruption over the years. As a result, farmers have received less than true market value for their livestock, and consumers have paid more than they should have paid for meat.

In an attempt to correct this situation and for other reasons, two companion proposals were published in late January with comments due by May 1. Five public hearings were held in March.

Public reaction to both proposals was quite negative and we are re-evaluating the specifics of each proposal. But we are convinced that changing the regulations which dictate the rules of the game in these two areas are important and will be in the long-run interest of both producers and consumers.

IV. Prospects for Remainder of 1978

Retail food price increases during the first half of 1978 have been higher than originally expected. The November 1977 Department of Agriculture estimate was that food prices in 1978 would average 6 percent higher than

in 1977. This estimate hinged importantly on the expected increase in pork production--which, primarily because of the extremely cold winter, did not materialize. Our expectation now is that prices in 1978 will average 8-10 percent higher than in 1977.

Food prices will likely continue to increase this summer, but at a much slower rate than during the spring. Supplies of several major produce items including potatoes, apples and citrus fruits are seasonally low during the summer months and their prices can be expected to increase. However, supplies of most other fresh fruits and vegetables will be at their seasonal peak. Although fresh produce prices are expected to be higher than last year, they will be contributing to the slower rate of food price increase this summer. By fall, seasonal declines in farm prices for most field crops, as well as for major fresh produce items, will likely offset increases in marketing costs and hold retail prices for foods derived from crops generally steady. Seasonably larger supplies of red meat and poultry may bring lower retail prices for these items by late fall. Further increases for eggs, dairy products and fish items will likely be offsetting, however. As a result of all these factors, we anticipate fourth quarter food prices to be about steady from their third quarter levels.

Mr. Chairman, that concludes my prepared testimony. If you have questions I will be happy to answer them. Thank you.

